February 5, 2020

The Honorable Maxine Waters
Chairwoman, House Committee on Financial Services
2129 Rayburn House Office Building
Washington, DC 20515

The Honorable Patrick McHenry
Ranking Member, House Committee on Financial Services
4340 O'Neill House Office Building
Washington, DC 20024

Re: Full Committee Hearing on "Rent-A-Bank Schemes and New Debt Traps: Assessing Efforts to Evade State Consumer Protections and Interest Rate Caps"

As the House Committee on Financial Services examines the different business practices of non-bank small-dollar loan providers, The Pew Charitable Trusts is offering comments on the potential benefits and risks to related to banks partnering with third parties to offer small-dollar credit. The Pew Charitable Trusts is a nonpartisan nonprofit organization that conducts research and promotes evidence-based public policy. Our consumer finance project supports policies that would improve the lives of families while creating a safe, more transparent marketplace for all.

These comments are informed by in-depth research Pew has conducted on the small-loan market since 2011. This research includes four nationally representative surveys of high-cost loan borrowers, 22 focus groups with borrowers of high-cost credit across the country, polls of the public, extensive analysis of market data and both state and federal regulatory data, and the laws of all 50 states. We have published reports, briefs, and fact sheets available on our website.

Consumers can benefit from bank small-dollar installment lending

Pew's research has found that if banks began offering small installment loans and lines of credit, they would have large comparative advantages over nonbank lenders, with their lower costs of doing business allowing them to offer loans profitably to many of the same borrowers at prices approximately six times lower than those of payday and other similar lenders.[1] Banks would be lending in a largely automated fashion to known customers who already make regular deposits, so acquisition and automated underwriting costs would be much lower than those of nonbank lenders. The cost of capital for banks is quite low, and their overhead costs are spread among the multiple products they sell. Small installment loans would expand banks' relationships with customers who until now have gone outside of the supervised and well-regulated banking system to borrow, and they may improve customer retention as well.[2] Furthermore, consumers borrowing from their bank would save billions a year in fees and interest, while avoiding the risks of non-bank predatory lenders.

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[1] The Pew Charitable Trusts, "Standards Needed for Safe Small Installment Loans from Banks, Credit Unions" (2018), 5, https://www.pewtrusts.org/en/research-and-analysis/issue-briefs/2018/02/standards-needed-for-safe-small-installment-loans-from-banks-credit-unions.

[2] Neil F. Hall, *American Banker*, "Banks Should Lead the Way to More Small-Dollar Loans" (2016), https://www.americanbanker.com/opinion/banks-should-lead-the-way-to-more-small-dollar-loans.

To offer affordable small-dollar installment loans to their own customers, we estimate that a large share of banks will turn to service providers who can help banks make these loans through mobile or online banking platforms. It would simply be impractical to build out such a program inhouse for all but the largest institutions. These partnerships can help banks offer small installment loans in largely automated fashion without requiring a hefty upfront investment or substantial staff time. Service providers that offer a white-labeled platform available through mobile or online banking are likely to substantially improve small and medium-sized banks' ability to offer small installment loans. This type of third-party relationship, as long as it is carefully monitored by the bank to ensure compliance with its standards and regulatory requirements, is likely to benefit consumers by making bank-issued, affordable loans available to them through the bank's online or mobile banking platform.

However, banks using their charters to originate high-cost loans via nonbank lenders, often called "rent-a-bank" arrangements, is entirely different and quite dangerous. Regulators should put an end to this harmful practice immediately. Third-party relationships where a payday or other non-bank lender uses a bank's charter to originate high-cost loans that would otherwise violate state usury laws put consumers at extreme risk. For example, payday and other high-cost lenders have issued single-payment and multi-payment loans with unaffordable terms at extremely high prices by partnering with banks that used their charters to preempt state price limits and other consumer protections. These loans and lines of credit are far more expensive than those that banks would offer to their own customers, and they have the effect of undermining state-level consumer safeguards. These kinds of relationships are nothing like banks using service providers to simplify lending to their own customers. We were pleased that the Office of the Comptroller of the Currency expressed in its May 2018 bulletin on small-dollar lending that it "views unfavorably" such relationships.[3]

We want to thank the Chairman and Ranking Member for allowing us to provide comments on this important policy discussion and to reiterate that banks issuing small-dollar credit to their own customers is a positive development if the installment loans and lines of credit have *fair prices, affordable payments, and reasonable time to repay*. Moreover, to accomplish this we estimate the majority of banks will rely on a third-party partnership in order to be able to lend to their own customers. Conversely, consumers will be at risk if third parties utilize bank charters to originate a high-rate loan that would otherwise violate state usury rate caps. Regulators should insist that banks immediately cease originating high-cost loans for nonbank lenders.

Sincerely,

Nick Bourke
Director, Consumer Finance
The Pew Charitable Trusts

[3] Office of the Comptroller of the Currency, U.S. Department of Treasury, "Description: Core Lending Principles for Short-Term, Small-Dollar Installment Lending," OCC Bulletin 2018-14, May 23, 2018, https://www.occ.gov/news-issuances/bulletins/2018/bulletin-2018-14.html.